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No. 430

IN THE

Supreme Court of the United States

October Term, 1951

Consumers Services, Inc., *Petitioner*,

v.

United States of America.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT.

Thurston Ravenel,
Attorney for the Petitioner.

c/o Ivins, Phillips & Barker,
815 Southern Building,
Washington 5, D. C.

Byron S. Adams, Washington, D. C.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1951.

No.

COMMUNITY SERVICES, INC., *Petitioner,*

v.

UNITED STATES OF AMERICA

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT.

Community Services, Inc., by its attorney, Fleming Bomar, prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Fourth Circuit, entered in this case May 5, 1951.

Opinions Below.

The opinion of the District Court (R. 2-21) is not reported in the Federal Supplement. The opinion of the Court of Appeals (R. 27-37) is reported in 189 F. (2d) 421.

Jurisdiction.

The judgment of the Court of Appeals was entered May 5, 1951. The Court of Appeals extended the time within which a petition for rehearing could be filed until June 18, 1951. (R. 38) On June 16, 1951 a petition for rehearing was filed (R. 40-54) which was considered by the Court of Appeals and denied June 19, 1951. (R. 55) On September 10, 1951, the Chief Justice granted an extension of time until November 16, 1951 within which a petition for writ of certiorari could be filed. (R. 57) The jurisdiction of this Court is invoked under 28 U. S. C. Section 1254(1).

Question Presented.

Whether a charitable corporation, the charter of which requires its entire net income to be expended exclusively for religious, charitable, scientific, literary and/or educational purposes, should be denied exemption from employment taxes during the period July 23, 1945 through December 31, 1947, solely because it derived its principal income from the sale of soft drinks, milk, candy, sandwiches and similar items to the employees of a textile mill and members of their families.

Statutes Involved.

The pertinent statutory provisions are printed in the Appendix, *infra*, pp. 9-10.

Statement.

The undisputed, pertinent facts found by the District Court (R. 2-8) may be summarized as follows:

Petitioner was incorporated on July 23, 1945 as a charitable corporation under the laws of the State of South Carolina. Petitioner has no capital stock. The charter of petitioner requires that all its "funds, properties and all profits so earned and derived therefrom shall be devoted exclusively to religious, charitable, scientific, literary

and/or educational purposes." The charter of petitioner also authorizes petitioner to own and operate various soft drink, milk, candy, sandwich and other concessions the customers of which are the employees of Graniteville Company and the people of the communities in which its mills are located.

Graniteville Company is a South Carolina corporation organized for the profit of its stockholders, which, since 1945, has been engaged continuously in the production and sale of cotton textile products. Its manufacturing plants are located in Graniteville, Warrenville, and Vaucluse, South Carolina, and in Augusta, Georgia, and during the period in question were operated on a 24-hour a day, three-shift basis, five days per week. In its operations Graniteville Company employs an average of about 5,000 personnel.

At the time of its incorporation, petitioner received a donation of $25,000 from Graniteville Company, and was authorized to operate all concessions formerly operated by Graniteville Company itself. Petitioner employed about 50 persons. Eighty-five percent of the gross receipts of petitioner were derived from the sale of soft drinks, milk, candy, and other similar item from wagons, pushed several times daily through Graniteville Company's plants by employees of petitioner. The remaining 15% of gross receipts were obtained from donations, and from the sale of ice, coal, gasoline and home appliances to employees of Graniteville Company and members of their families in communities where such items were otherwise unobtainable.

Petitioner owns no land or buildings.

None of the members, officers or directors of petitioner have ever received any compensation for services rendered to petitioner.

The net income of petitioner has been distributed, as its charter requires, for religious, charitable and educational purposes. Any net income which was not distributed currently for such purposes was reserved to pay any taxes adjudged to be due the Government if this litigation ends

unsuccessfully. Local churches, schools and charities in Aiken County, South Carolina, are the principal recipients of the net income of petitioner.

From the date of its incorporation through December 31, 1949, the operating income of petitioner totalled $85,215.66; of this sum $48,051.00 was distributed to local churches, schools and charities, and the remaining net income was undistributed, as of December 31, 1949.

Following receipt of a ruling from the Commissioner of Internal Revenue that petitioner did not qualify for tax exemption under the provisions of section 101(6) of the Internal Revenue Code, petitioner filed, under protest, employment tax returns for the period July 23, 1945 to December 31, 1947, paid employment taxes totalling $3,910.16 for such period to the Collector of Internal Revenue, Columbia, South Carolina, and brought this suit for refund. The District Court held that petitioner was exempt from such taxes and ordered the refund. The Court of Appeals for the Fourth Circuit reversed.

Reasons for Granting the Writ.

1. A conceded conflict of decisions among Courts of Appeals in several circuits is the primary reason for granting this petition. In its decision herein, the Court of Appeals for the Fourth Circuit admits that its conclusions are in conflict with the decision of the Court of Appeals for the Second Circuit in *Roche's Beach, Inc.* v. *Commissioner*, 96 F. (2d) 776. Said the court:

> "The majority opinion in *Roche's Beach Inc.* holds squarely in favor of taxpayer. The force of that case, however, is greatly weakened by the strong dissent of Judge Learned Hand, with which we heartily agree. . . ."

The decision is also in direct and irreconcilable conflict with the decision of the Court of Appeals for the Fifth Circuit in *Willingham* v. *Home Oil Mill*, 181 F. (2d) 9, certiorari denied 340 U. S. 852; and with the decision of

the Court of Appeals for the Sixth Circuit in *Commissioner* v. *Edward Orton, Jr. Ceramics Foundation*, 173 F. (2d) 483.

On June 20, 1951, subsequent to the date on which the Fourth Circuit decided the case at bar, the Court of Appeals for the Third Circuit in *C. F. Mueller Company* v. *Commissioner*, 190 F. (2d) 120, rendered a decision which also is in direct conflict with the decision in the instant case, the Third Circuit regarding the Second Circuit's decision of *Roche's Beach, Inc.* v. *Commissioner, supra*, as still the law.

The decision in the instant case is also contrary, in principle, to these additional decisions of the Court of Appeals for the Second and Fifth Circuits: *Commissioner* v. *Battle Creek, Inc.*, 126 F. (2d) 405 (5th Circuit 1942); *Bohemian Gymnastic Assoc. Sokol* v. *Higgins*, 147 F. (2d) 774 (2nd Circuit 1945); *Debs Memorial Radio Fund* v. *Commissioner*, 148 F. (2d) 948. The decision against petitioner is also contrary to that of the Court of Claims in *Southeastern Fair Association* v. *United States*, 52 F. Supp. 219.

It is likewise in conflict with the very recent (not yet published in the Federal Reporter) decision of the Court of Appeals for the Ninth Circuit in *Squire* v. *Students Book Corporation*, decided October 17, 1951; 51-5 C. C. H. ¶ 9473.

2. The decision below conflicts with the decision of this Court in *Trinidad* v. *Sagrada Orden de Predicadores*, 263 U. S. 578, T. D. 3548 III-1CB 270. Twenty-seven years ago, this Court interpreted a tax exemption statute containing the same language as the statute in issue. In the *Trinidad* case (1924), the principle was enunciated that, in determining whether an organization was organized and operated exclusively for religious, charitable, scientific, literary or educational purposes, the destination of its income, and not the source thereof, constituted the "ultimate test of exemption." The fact that a corporation, otherwise exempt, derived income from real estate, loans, investments and from the sale of candy, chocolate and the like was held not to deprive it of its exemption, if the income so derived was devoted to exempt purposes.

The decision in the *Trinidad* case has been consistently interpreted by all the Courts of Appeals having occasion to cite it until the case in issue.

Exemption has been denied by the Courts of Appeals generally speaking where the charter of a corporation did not require its income to be devoted to charity, even though its stock had been subsequently acquired by a concededly exempt institution. *Sun-Herald Corporation* v. *Duggan*, 160 F. (2d) 475 (C. C. A. 2nd); *Bear Gulch Water Works Co.* v. *Commissioner*, 116 F. (2d) 975; *Gagne* v. *Hanover Water Works Company*, 92 F. (2d) 659. *Contra: Squire* v. *Students Book Corporation, supra.*

Exemption has uniformly been denied where the income of a corporation inured to the benefit of private individuals or where one of the purposes of the corporation was the selfish purpose of benefiting its incorporators. *Better Business Bureau of Washington, D. C., Inc.* v. *United States*, 326 U. S. 279 (1945); *Universal Oil Products Company* v. *Campbell*, 181 F. (2d) 451 (7th Circuit 1950); *Davenport Foundation* v. *Commissioner*, 170 F. (2d) 70; *Underwriters Laboratories, Inc.* v. *Commissioner*, 135 F. (2d) 371; *Scholarship Endowment Foundation* v. *Nicholas*, 106 F. (2d) 552.

But exemption has never been denied, until the instant case, on account of the source of the income of a corporation, if its charter required all income to be devoted, and if such income was or had to be devoted, exclusively to religious, charitable, scientific, literary or educational purposes.

3. The Commissioner of Internal Revenue approved, originally, the majority decision of the Court of Appeals for the Second Circuit in *Roche's Beach, Inc., supra*, holding that a corporation whose activities included the operation of a commercial beach resort was tax exempt because its income had to be turned over to a charitable foundation. The decision was published as a court decision (Ct. D. 1359, 1938-2 CB 230) for the guidance of Bureau personnel and its conclusions were approved in opinions of the General Counsel of the Bureau (G. C. M. 20853, 1938-2 CB 166;

G. C. M. 21610, 1939-2 CB 103; G. C. M. 22116, 1940-2 CB 100). In 1942, G. C. M. 23063 (1942-1 CB 103) was published by the Commissioner, reversing the rulings of 1938, 1939 and 1940. This was done to avoid embarrassment to Government counsel arguing the case of *Commissioner* v. *Battle Creek, Inc., supra,* in the Fifth Circuit Court of Appeals. After the Fifth Circuit followed the *Roche's Beach* decision, and the Congress ignored Treasury recommendations for amendment to the statute, the Bureau of Internal Revenue continued to follow the *Roche's Beach* rule in many cases without publishing new Bureau rulings. Finally, in 1948, the Bureau established a policy of forcing to litigation the tax exempt status of any charitable corporation which was considered to be engaged in competitive business even though its income was devoted to charity. The Bureau was completely unsuccessful in it endeavor to obtain a decision from a court of appeals contrary to the majority opinion in *Roche's Beach, Inc.* until the decision of the Fourth Circuit in the instant case.

Since the conflict is conceded, the case at bar presents a suitable vehicle to resolve the question of whether a charitable corporation should be denied the tax exempt status it would otherwise have enjoyed (until Congress changed the law, effective in 1951) both from employment taxes and federal income taxes, merely because it derives income from commercial business as contrasted with investments.

It is agreed that the decisions of the Courts of Appeals interpreting the income tax exemption granted under section 101(6) of the Internal Revenue Code are not only pertinent but controlling in the interpretation of the exemption from employment taxes contained in section 1426(b)(8) of the Internal Revenue Code.

4. By Title III of the Revenue Act of 1950, Congress changed the federal income tax laws prospectively for charitable organizations. Income of charities from certain sources is now taxed, while income from other sources is

not. Section 303 of the Revenue Act of 1950, describing the effective date of such changes provides:

> "The amendments made by this part shall be applicable only with respect to taxable years beginning after December 31, 1950. The determination as to whether an organization is exempt under section 101 of the Internal Revenue Code from taxation for any taxable year beginning before January 1, 1951, shall be made as if section 301(b) of this Act had not been enacted and without inferences drawn from the fact that the amendment made by such section is not expressly made applicable with respect to taxable years beginning before January 1, 1951."

The question presented herein is nevertheless very important to many organizations insofar as tax liabilities for years prior to 1951 are concerned. Furthermore, Congress seems to have expected that the law for the years prior to 1951, in cases such as this, would be settled by the Supreme Court.[1]

Conclusion.

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Respectfully submitted,

FLEMING BOMAR,
Attorney for the Petitioner.

c/o IVINS, PHILLIPS & BARKER,
306 Southern Building,
Washington 5, D. C.

November, 1951.

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[1] Cf. Report of House Committee on Ways and Means (HR 2319, 81st Cong. 2d Sess., p. 124): "In the area covered by this amendment there has been litigation as to the application of such a rule under existing law (cf. *Roche's Beach, Inc.* v. *Commissioner*, C.C.A. 2, 1938), 96 F. (2d) 776; *Universal Oil Products Co.* v. *Campbell*, (C.A. 7, 1950), 181 F. (2d) 451; *Willingham* v. *Home Oil Mill* (C.A. 5, 1950), 181 F. (2d) 9; *C. F. Mueller Co.*, 14 T. C. No. 111-½ (May 25, 1950)). The amendment is intended to show clearly what, from its effective date, the rule is to be, without disturbing the determination in present litigation of the rule of existing law."

APPENDIX.

Internal Revenue Code (prior to 1950 amendments)

[Income tax]

SEC. 101. Exemptions from Tax on Corporations. The following organizations shall be exempt from taxation under this chapter—

(6) Corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, and no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation;

* * *

[Employment tax]

SEC. 1410. Rate of Tax.

In addition to other taxes, every employer shall pay an excise tax, with respect to having individuals in his employ, equal to the following percentages of the wages (as defined in Section 1426(a)) paid by him after December 31, 1936, with respect to employment (as defined in section 1426(b)) after such date:

(1) [As amended by Sec. 2 of the Social Security Act Amendments of 1947, c. 510, 61 Stat. 793]. With respect to wages paid during the calendar years 1939 to 1949, both inclusive, the rate shall be 1 per centum.

* * *

(26 U. S. C. 1946 ed., Sec. 1410.)

[Employment tax]

SEC. 1426. Definitions.

* * *

(b) Employment.—The term "employment" means * * * any service, of whatever nature, performed after December 31, 1939, by an employee for the person employing him * * * except—

* * *

(8) [As amended by Sec. 606 of the Social Security Act Amendments of 1939, c. 666, 53 Stat. 1360] Service performed in the employ of a corporation, community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, literary or educational purposes, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, and no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation;

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In the Supreme Court of the United States

OCTOBER TERM, 1951

No. 430

COMMUNITY SERVICES, INC., PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

MEMORANDUM FOR THE UNITED STATES

OPINIONS BELOW

The opinion of the District Court (R. 2-22) is not reported. The opinion of the Court of Appeals (R. 27-37) is reported at 189 F. 2d 421.

JURISDICTION

The judgment of the Court of Appeals was entered on May 5, 1951. (R. 38.) Taxpayer's petition for rehearing was denied on June 19, 1951. (R. 55.) By order of the Chief Justice, the time

for filing a petition for a writ of certiorari was extended to November 16, 1951. (R. 57.) The petition for a writ of certiorari was filed on November 16, 1951. The jurisdiction of this Court is invoked under 28 U.S.C., Section 1254.

QUESTION PRESENTED

Whether a corporation engaging in ordinary business activity for profit is exempt from employment taxes under Section 1426(b)(8) of the Internal Revenue Code solely by reason of the fact that its profits are payable to exempt organizations.

STATUTE AND REGULATIONS INVOLVED

These appear in the Appendix, *infra*, pp. 11-14.

STATEMENT

The material facts are stipulated and were incorporated as stipulated in the District Court's opinion. (R. 3-8.) They may be summarized as follows:

Taxpayer corporation was organized on July 23, 1945, as a non-stock membership corporation under the laws of South Carolina. (R. 3.) Its charter states (Stip. Ex. 1, R. 22):

> FOURTH: The purpose of the said proposed corporation is to receive donations of cash and properties through gift, bequest, devise or otherwise, and to own and operate a canteen refreshment service and other business ventures for the convenience of the employees of Graniteville Company and the people of the communities in which its mills are operated,

> and to conduct other businesses in order to earn profits, to the end that all funds, properties, and all profits so earned and derived therefrom shall be devoted exclusively to religious, charitable, scientific, literary and/or educational purposes.

The by-laws of the corporation recite the same purposes (Stip. Ex. 2, R. 22-23) and further provide that (R. 23):

> The nature, extent and location of the canteen refreshment service, other business ventures and businesses of the Corporation, and the details of the devoting of its net profits to the objects set out in the charter of the Corporation and the choosing of such objects and the beneficiaries of the bounty of the corporation; and all details connected with the operations and activities of the corporation are to be determined from time to time, as the exigencies of the business of the Corporation require, by the Board of Directors, subject always to the provisions of Section 2 of this Article.

The members of the corporation throughout the taxable period (July 23, 1945-December 31, 1947), who also constituted its board of directors, were the president, vice-president, and two other executives of the Graniteville Company, and a civic leader in the community. (R. 3.) The Graniteville Company is a textile manufacturing corporation having its principal office and plants in Graniteville, South Carolina, and it employs about 5,000 persons. (R. 4.)

Prior to taxpayer's formation, the Graniteville Company operated a canteen refreshment service in its various plants, and also sold coal and ice to its employees. (R. 7.) On the day taxpayer was organized, the Graniteville Company donated to it $25,000, and authorized it to operate all concessions previously operated by Graniteville. Thereafter, and during the taxable period, taxpayer operated a canteen refreshment service, a coal and wood yard, a filling station, and an electrical appliance store. Eighty-five percent of its gross receipts was derived from the sale of soft drinks, milk, candy, sandwiches and similar items to employees of Graniteville Company. The balance of its gross receipts was derived from the sale of coal, ice, gasoline, and home appliances to Graniteville Company's employees and their families. No sales were made to the general public. Taxpayer also leased from the Graniteville Company at a nominal rental a filling station and a dining room, both of which were operated by taxpayer during 1945. Thereafter, taxpayer sublet the filling station and dining room at a profit to one Reeves, who operated them as tenant of taxpayer. All of taxpayer's operations were conducted on properties owned by, or leased from, Graniteville Company. Taxpayer's officers and directors received no compensation. To carry on its business, taxpayer employed about fifty persons, who received salaries and wages of $26,658 in 1945, $85,765 in 1946, $92,-

051 in 1947, and $102,853 in 1948. (R. 4-5; Stip. Ex. 3, R. 24.)

From the date of its incorporation in July of 1945 to the end of that year, taxpayer had a small ($482) operating loss. For 1946, its net profits amounted to $3,492, no part of which was contributed to charitable or like institutions. For 1947, its net profits amounted to $19,381, of which $3,696 was contributed to charitable and educational institutions. For 1948, its net profits amounted to $37,738 (including contributions totaling $550), of which $9,865 was contributed to charitable institutions. (R. 5-6, 24.) Taxpayer's total receipts exceeded total disbursements by $24,517 in 1945, by $3,492 in 1946, by $15,865 in 1947, and by $27,873 in 1948. (R. 24.) It retained this excess as a reserve against taxes which might be adjudged due to the Government. (R. 8.)

Taxpayer filed employment tax returns under the Federal Insurance Contributions Act (subchapter A of chapter 9 of the Internal Revenue Code) for the period July 23, 1945, to December 31, 1947, and paid employment taxes totaling $3,910.16 for this period. Thereafter, it filed a claim for refund on the ground that it was exempt from tax under Section 1426(b)(8) of the Internal Revenue Code. The claim for refund was denied, and taxpayer instituted suit for refund. (R. 6.) The District Court held "as a matter of law" that taxpayer was exempt from employment taxes under Section

1426(b)(8). (R. 21.) It so held on the theory that a corporation organized and operated for the purpose of carrying on business for profit is "organized and operated exclusively for * * * charitable * * * purposes" within the meaning of Section 1426(b)(8), if its profits are destined for charitable organizations. (R. 9-22.) The Court of Appeals reversed. (R. 27-37.)

DISCUSSION

1. The decision below is in complete accord with the decision of this Court in *Better Business Bureau* v. *United States*, 326 U.S. 279. This Court there held that a corporation organized for the purpose of improving business ethics did not qualify for exemption from employment tax as an "educational" organization under Section 811 (b)(8) of the Social Security Act, the forerunner of Section 1426(b)(8) of the Internal Revenue Code (Appendix, *infra*, pp. 11-12) here involved,[1] notwithstanding that no part of its earnings inured to the benefit of any private person and that it was organized under local law as an educational organization. It so held on the ground that the corporation was not "organized and operated exclusively" for educational purposes, within the meaning of the statute, since a part of its activities were aimed at promoting a profitable business community.

[1] Code Section 1426(b)(8) is derived from and in all material respects is the same as Section 811(b)(8) of the Social Security Act of 1935, c. 531, 49 Stat. 620.

The rationale of the decision in the *Better Business Bureau* case applies with even greater force here, since no part of taxpayer's activities were educational or charitable. They consisted entirely of operating various business enterprises in the community.[2] (R. 4-5, 24.) That taxpayer's business profits were destined for charitable or educational institutions is no more significant here than was the stipulated fact in the *Better Business Bureau* case (326 U.S. at 281) that no part of the taxpayer's earnings inured to the benefit of any private shareholder or individual. The corporation claiming exemption, as distinguished from its stockholders or other recipients of its income, must be "organized and operated exclusively" for the specified statutory purposes. See Section 402.215 of Treasury Regulations 106 (Appendix, *infra*, pp. 12-14). "This plainly means that the presence of a single noneducational purpose, if substantial in nature, will destroy the exemption * * *." *Better Business Bureau* v. *United States, supra*, p. 283.

2. Taxpayer alleges conflict (Pet. 4-6) with several decisions involving the question of income tax exemption under Section 101(6) of the Internal Revenue Code, the language of which is substan-

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[2] Nor was taxpayer "organized" exclusively for charitable or like purposes. Its charter broadly empowered it to carry on business for profit. (R. 22.)

tially the same as that of Section 1426(b)(8).[3] The conflict does exist, but recent legislation has rendered it completely academic with respect to taxable years after 1950, and partly academic with respect to prior years.

Section 301(b) of the Revenue Act of 1950, c. 994, 64 Stat. 910, added to Code Section 101 a new paragraph, applicable to taxable years after 1950, expressly denying income tax exemption to "feeder" organizations, that is, those carrying on a business for profit and whose profits inure exclusively to organizations exempt under Section 101.[4] With respect to prior years, Section 302(b) of the same Act provides in substance that no tax may be asserted for any year prior to 1947 unless a deficiency had already been asserted, or the tax had already been assessed or paid. See H. Rep. No. 2319, 81st Cong., 2d Sess., pp. 36-37, 41-42, 124 (1950-2 Cum. Bull. 380, 408-409, 412, 469); S. Rep. No. 2375, 81st Congress, 2d Sess., pp. 35-36 (1950-2 Cum. Bull. 483, 509). Furthermore, Section 601 of the Revenue Act of 1951, Public Law 183, 82nd Cong., 1st

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[3] While the language of the two sections is the same, certain corporations which might qualify for income tax exemption are not necessarily entitled to employment tax exemption. See *Better Business Bureau* v. *United States*, 326 U.S. at 284-285; Code Section 1426(b)(10)(A) (Appendix, *infra*, p. 12).

[4] This paragraph provides that—

> An organization operated for the primary purpose of carrying on a trade or business for profit shall not be exempt under any paragraph of this section on the ground that all of its profits are payable to one or more organizations exempt under this section from taxation. * * *

Sess., amended Section 302 of the 1950 Act so as specifically to exempt for any prior year "feeder" organizations whose profits inured solely to the benefit of a regularly established educational or hospital institution.[5] See also H. Rep. No. 586, 82d Cong., 1st Sess., pp. 35-36; S. Rep. No. 781, 82d Cong., 1st Sess., pp. 29-30; H. Conference Rep. No. 1179, 82d Cong., 1st Sess., p. 104.

Thus, the 1950 Revenue Act has disposed of the question with respect to future taxable years and as to all types of "feeder" organizations; the 1951 Act has disposed of it with respect to prior years as to educational and hospital "feeder" organizations. Accordingly, review of this case could serve only to resolve the question in the narrow class of cases remaining in this field, namely, those involving the claimed exemption of a non-educational or non-hospital "feeder" organization for a taxable year prior to 1951. See *supra*, p. 8.

However, the Commissioner of Internal Revenue has advised the Department of Justice that "there are a number of open cases presenting the issue whether an organization is entitled to exemption by virtue of the fact that its income is distributable to a charitable institution other than a hospital or educational institution" and that, in his view, the

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[5] The enactment of this section has rendered academic the question presented in *C. F. Mueller Co.* v. *Commissioner*, 190 F. 2d 120 (C.A. 3d), and *Squire* v. *Students Book Corp.* (C.A. 9th), decided October 17, 1951 (1951 C.C.H., par. 9473), upon which taxpayer relies for conflict. (Pet. 5.)

matter remains of sufficient importance to make "a decision of the Supreme Court desirable".[6]

Though, as previously indicated, the importance of the issue tendered by the petition for a writ of certiorari has been greatly diminished by recent legislation, the Government does not feel that it can, in the circumstances, oppose the issuance of a writ of certiorari in this case.

Respectfully submitted,

PHILIP B. PERLMAN,
Solicitor General.

JANUARY, 1952

[6] Letter, dated January 9, 1952, from Commissioner John B. Dunlap to Acting Assistant Attorney General Ellis Slack.

APPENDIX

Internal Revenue Code:

SEC. 1410. RATE OF TAX.

In addition to other taxes, every employer shall pay an excise tax, with respect to having individuals in his employ, equal to the following percentages of the wages (as defined in section 1426(a)) paid by him after December 31, 1936, with respect to employment (as defined in section 1426(b)) after such date:

(1) [As amended by Sec. 2 of the Social Security Act Amendments of 1947, c. 510, 61 Stat. 793.] With respect to wages paid during the calendar years 1939 to 1949, both inclusive, the rate shall be 1 per centum.

* * * * *

(26 U.S.C. 1946 ed., and Supp. IV, Sec. 1410.)

SEC. 1426. DEFINITIONS.

* * * * *

(b) [As amended by Sec. 606 of the Social Security Act Amendments of 1939, c. 666, 53 Stat. 1360.] *Employment.*—The term "employment" means * * * any service, of whatever nature, performed after December 31, 1939, by an employee for the person employing him * * * except—

* * * * *

(8) Service performed in the employ of a corporation, community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, literary, or

educational purposes, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, and no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation;

* * * * *

(10) (A) Service performed in any calendar quarter in the employ of any organization exempt from income tax under section 101, if—

(i) the remuneration for such service does not exceed $45, or

* * * * *

(26 U.S.C. 1946 ed., Sec. 1426.)

Treasury Regulations 106, promulgated under the Internal Revenue Code:

Sec. 402.215. *Religious, charitable, scientific, literary, and educational organizations and community chests.*—Services performed by an employee in the employ of an organization of the class specified in section 1426(b)(8) of the Act are excepted.

For purposes of this exception the nature of the services performed is immaterial; the statutory test is the character of the organization for which the services are performed.

In all cases, in order to establish its status under the statutory classification, the organization must meet the following three tests:

(1) It must be organized and operated exclusively for one or more of the specified purposes;

(2) Its net income must not inure in whole or in part to the benefit of private shareholders or individuals; and

(3) It must not by any substantial part of its activities attempt to influence legislation by propaganda or otherwise.

Corporations or other institutions organized and operated exclusively for charitable purposes comprise, in general, organizations for the relief of the poor. The fact that an organization established for the relief of indigent persons may receive voluntary contributions from the persons intended to be relieved will not necessarily affect its status under the law.

An educational organization within the meaning of section 1426(b)(8) of the Act is one designed primarily for the improvement or development of the capabilities of the individual * * *.

Since a corporation or other institution to be within the prescribed class must be organized and operated exclusively for one or more of the specified purposes, an organization which has certain religious purposes and which also manufactures and sells articles to the public for profit is not within the statutory class even though its property is held in common and its profits do not inure to the benefit of individual members of the organization.

An organization otherwise within the statutory class does not lose its status as such by receiving income such as rent, dividends, and interest from investments, provided such income is devoted exclusively to one or more of the specified purposes.

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IN THE

Supreme Court of the United States

October Term, 1951

No. 430

COMMUNITY SERVICES, INC., *Petitioner,*

v.

UNITED STATES OF AMERICA.

PETITION FOR REHEARING.

On February 4, 1952, the Supreme Court of the United States handed down an order denying petitioner's application for writ of certiorari in the above-described case. By order of the Chief Justice dated February 12, 1952, the time for filing a petition for rehearing was extended to and including February 25, 1952.

Petitioner's application for writ of certiorari was denied even though grounded upon a conceded conflict of decisions among the United States Courts of Appeals[1]. It was

[1] Judge Dobie in the case at bar admitted disagreement with *Roche's Beach, Inc.* v. *Commissioner* (CCA 2nd) 96 F. (2d) 776. The decision of the Fourth Circuit in the case at bar is also in direct conflict with that of the Third Circuit in *C. F. Mueller Co.* v. *Commissioner*, 190 F. (2d) 120; the Fifth Circuit in *Willingham* v. *Home Oil Mill*, 181 F. (2d) 9 (1950); and the Sixth Circuit in *Commissioner* v. *Edward Orton, Jr. Ceramics Foundation*, 173 F. (2d) 483 (1949); and others.

denied even though unopposed by the Government[2]. Presumably the denial was based upon representations of the Government that recent legislation has rendered unimportant the question in issue.

Existing grounds for reconsideration not previously presented are:

1. The continued importance of the question in issue is clearly demonstrated by the following list of cases[3] which are still pending in the Tax Court, the United States District Courts, the Court of Claims, and the United States Courts of Appeals, and which involve the identical issue presented in petitioner's application for writ of certiorari. None of these cases is affected by Section 601(a) of the Revenue Act of 1951.

(a) Cases docketed in the Tax Court of the United States which have not been decided:

Shattuck-Ohio Foundation, Docket No. 37057, filed October 3, 1951—Minneapolis, Minnesota
C. F. Smith Company, Docket No. 32973, filed March 8, 1951—Los Angeles, California
William L. Powell Foundation, Docket No. 35422, filed June 25, 1951, Indianapolis, Indiana
John Danz Charitable Trust, Docket No. 33429, filed April 9, 1951—Seattle, Washington
John Danz Charitable Trust, Docket No. 26404, filed January 9, 1950—Seattle, Washington
Youth Trust, Inc., Docket No. 32201, Docket No. 32200, and Docket No. 32199, filed January 15, 1951—Detroit, Michigan
John H. Lickert, Docket No. 32217 and Docket No. 32218, filed January 15, 1951—Detroit, Michigan
Ralph H. Eaton Foundation, Docket No. 30985, filed October 12, 1950—Los Angeles, California
Rio Farms, Inc., Docket No. 26948, filed February 23, 1950—Houston, Texas

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[2] Memorandum for the United States (p. 10).

[3] A similar list was transmitted by the Treasury Department to the Department of Justice with its recommendation in favor of review by certiorari.

Gemological Institute of America, Docket No. 26183, filed December 16, 1949—Los Angeles, California
Arthur Jordan Foundation, Docket No. 31263, filed November 6, 1950—Indianapolis, Indiana
American Association of Engineers, Inc., Docket No. 22919, filed May 6, 1949—Chicago, Illinois

(b) Cases docketed in the United States District Courts which have not been decided:

Sebastian Lathe Co. v. *Johnson, Collector* (S.D., N.Y.)
Rio Farms, Inc. v. *Scofield, Collector* (W.D., Texas)

(c) Cases decided by the Tax Court, now on appeal:

Donor Realty Corporation, 17 T.C. —— No. 107 (November 29, 1951) Appealed to C.A. 2nd

(d) Cases decided by the United States District Courts, the time for appeal not having expired:

Jack Little Foundation for Aid to the Deaf v. *Jones, Collector* (W.D., Oklahoma, December 10, 1951) —— F. Supp. ——

(e) Cases decided by the Court of Claims, the time for filing application for writ of certiorari not having expired:

The Sico Company v. *United States*, —— F. Supp. —— (Court of Claims, January 8, 1952)

While the above-described list of cases pending before the Tax Court and Court of Appeals is reasonably complete, the list of cases pending before the United States District Courts and the Court of Claims is necessarily incomplete because of the fact that the Justice Department is considerably behind in compiling statistics of the types of cases pending in the District Courts and the Court of Claims.

Furthermore, it is obviously impossible to ascertain the number of cases in which the issue has been raised but which are not yet docketed in court. It is reasonable to assume that since the Treasury Department has not had

time to audit tax returns in all sections of the country for the years 1947, 1948, 1949 and 1950, many additional cases involving the identical issue will be brought to light at the time such audits are made.

2. The second existing ground for reconsideration is that subsequent to the date on which petitioner filed its application for writ of certiorari, the Court of Claims rendered its decision in *The Sico Company* v. *United States* (not yet reported in Federal Supplement) decided January 8, 1952, which decision involves the identical issue presented in the instant case and which decision is diametrically opposed to the decision of the Court of Appeals for the Fourth Circuit in the case at bar. In its unanimous decision, the Court of Claims stated,

> "In the case of *United States* v. *Community Services, Inc.*, 189 Fed. (2d) 421, the court held, in effect, that the source rather than the destination of the income should be the determining factor in the interpretation of the tax-exemption provision of the statute relating to the exemption from taxation of corporations organized and operated exclusively for religious, charitable, scientific, literary or educational *purposes*. We have carefully considered the court's opinion in that case but we are unable to concur in the conclusion reached therein, for the reasons well-stated in *C. F. Mueller Co.* v. *Commissioner*, 190 Fed. 2d 120, with which we agree."

The decision of the Court of Claims in the *Sico Company* case presents an "intervening circumstance" of substantial effect.

3. The decision of this court in *Better Business Bureau* v. *United States*, 326 U. S. 379 (decided November 13, 1945) strongly relied upon in the Solicitor General's "Memorandum for the United States" (pp. 6-7) and the Court of Appeals for the Fourth Circuit, offers no justification whatever for denying certiorari in the case at bar. The *Better Business Bureau* decision did not involve the exemption of

charitable feeder organizations deriving income from competitive business activities. The Better Business Bureau derived no income from operating a business. It had no income except dues. The question raised was whether its dues were used for "educational purposes" exclusively, or for the non-educational purpose of promoting a better business climate for the dues paying members. This court found the latter to be the case.

By contrast, petitioner devoted its net income exclusively to charitable purposes. Petitioner was denied exemption nevertheless because of the source of such income. The two questions are entirely different.

4. Finally, a decision of this court in the case at bar would resolve a broader issue than has been indicated by the Government. The "Memorandum for the United States" filed in response to our petition for certiorari, says at page 9:

> "Thus the 1950 Revenue Act has disposed of the question with respect to future taxable years * * *, the 1951 Act has disposed of it with respect to prior years as to educational and hospital 'feeder' organizations."

The above-quoted statement is not correct. While Section 601(a) of the Revenue Act of 1951 granted retroactive exemption from *income* taxes to certain educational and hospital "feeder" organizations, it granted no exemptions whatever from *employment* taxes. The case at bar involves *employment* taxes, as does the recent decision of the Court of Claims in *The Sico Company*.

Thus, the question at issue in the case at bar has not been disposed of by legislation for any organizations for years prior to 1951.

While the Justice Department could not well recommend certiorari in *C. F. Mueller Co.* v. *Commissioner*, 190 F. (2d) 120, an *income* tax case, it could recommend certiorari in

the *Sico Company*[4] case, where *employment* taxes are involved, and where the issue is legally identical with that in the case at bar.

Whether or not certiorari is requested in the *Sico Company* case, a decision of this court in the case at bar would be most desirable in order to settle for all years prior to 1951 the employment tax issue for all eleemosynary organizations which derived income from business activities, as well as the income tax issue for all such organizations who distributed their income to the many worthwhile charities other than schools or hospitals.

Such questions have not been and will not be resolved in a consistent manner in the various Courts of Appeals in the absence of a decision of this court.

WHEREFORE, PETITIONER RESPECTFULLY requests reconsideration of its petition for writ of certiorari, and for the additional reasons recited herein, prays that such writ be granted.

Respectfully submitted,

FLEMING BOMAR,
Attorney for the Petitioner.

c/o IVINS, PHILLIPS & BARKER,
306 Southern Building,
Washington 5, D. C.

February, 1952.

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[4] A petition for writ of certiorari in the *Sico Company* case must be filed prior to April 7, 1952, unless an extension of time is obtained by the Government.

IN THE

Supreme Court of the United States

October Term, 1951

No. 430

COMMUNITY SERVICES, INC., *Petitioner,*

v.

UNITED STATES OF AMERICA.

Certificate of Counsel.

I, FLEMING BOMAR, counsel for petitioner in the above-described case, do hereby certify that the attached petition for rehearing is presented in good faith and not for delay; and that the petition is restricted to the grounds above specified.

FLEMING BOMAR,
Attorney for Community Services, Inc.

Subscribed and sworn to before me this 21st day of February, 1952.

HELEN E. BLISS,
Notary Public.

My commission expires October 7, 1952.